

## **NOPOOR**

### ***Enhancing Knowledge for Renewed Policies against Poverty***

**SP1 Cooperation- Collaborative project- SICA**

**Grant Agreement no: 290752**

**FP7-SSH-2011-1**

### ***DELIVERABLE 4.3 (WP 4)***

**Title:** Report on Strategies and Performance of New Donors  
**Work package:** Impact of International Aid on Poverty (WP4)  
**Due date of deliverable:** 30<sup>th</sup> of September 2015  
**Actual submission date:** 1<sup>st</sup> of October 2015  
**Start date of project:** **1st April 2012**  
**Duration:** **60 months**  
**Organisation name of lead :** CRED  
**Contractor of this deliverable:** Jean-Philippe Platteau  
**Author (s):** Jean-Philippe Platteau  
**With the help of:** Marie Boltz and Jérémie Gross  
**Nature:** **Report**

<b>Project co-funded by the European Commission within the Seventh Framework Programme (2007-2013)</b>		
<b>Dissemination Level</b>		
<b>PU</b>	Public	<b>X</b>
<b>PP</b>	Restricted to other programme participants (including the Commission Services)	
<b>RE</b>	Restricted to a group specified by the consortium (including the Commission Services)	
<b>CO</b>	Confidential, only for members of the consortium (including the Commission Services)	

## WP 4 – TASK 4.3

### Report on Strategies and Performance of New Donors

- 1) NGOs have the advantage of getting into direct contact with the beneficiary populations, outside the official channel and its associated constraints. Moreover, some of them devote the whole or a part of their effort to advocacy activities that aim at making the government more accountable of its citizens. To the extent that advocacy efforts have the effect of decreasing corruption, there is an obvious spillover from such efforts to the effective mess of aid-on-the-ground.
- 2) Because they have the character of a public good, advocacy activities will be under-supplied by the NGOs which have a fixed amount of aid money to allocate between advocacy and direct aid to beneficiary populations (or by NGOs which are specialized in advocacy and have a flexible amount of money to spend). If NGOs are able to coordinate their efforts, however, they will cause direct aid transfers to be reduced owing to the induced repression of the local government whose rents are being threatened. For this reason, it is not desirable to rely entirely on the NGOs sector's efforts to improve local governance. This means that the governments of donor countries cannot eschew their duties to complement the advocacy efforts of NGOs.
- 3) The danger that new donor countries will not joined the coordinated efforts of old donors to impose governance-related conditionalities on recipient countries may be over-estimated.
- 4) In their direct aid efforts, NGOs may evince a number of weaknesses. In particular, they may follow a herd behaviour that prevents them from optimally locating their development projects on the ground. Moreover, there is no clear evidence that they better target the poor than public assistance efforts.
- 5) The need to produce visible results in rather short periods of time to persuade their fund-providers to renew their support distorts the allocation decisions of the NGOs. Long-term development efforts along not easily measurable dimensions are at the risk

of being neglected. This applies not only to NGOs that implement development projects but also to Civil Society Organisations (CSOs). Regarding the latter, the problem arises that the funding agencies not only have a short-term horizon but also do not get a proper understanding of the advocacy mission of the CSOs. Funding organisations such as the European Union should therefore aim at devising measures of the effectiveness of NGOs that are appropriate to their specific mission, and at enforcing decisions based on them. The former objective implies that (i) inputs or effort measures are taken into consideration (payment by results is not necessarily adequate), and that (ii) the way intermediary objectives are achieved should be measured and used as the basis of decisions.

- 6) The existence of scale economies in fundraising activities tends to cause a growing concentration or integration of NGOs. The positive aspect is that the adverse effects of acute competition among NGOs for aid funds are averted, especially if the aggregate amount of funds available for aid is more or less fixed. The negative side is that the variety of services offered by the NGOs may thereby be hampered. It is therefore important to study more carefully the experiences of countries, such as Belgium, where the NGO sector is being increasingly coordinated, yet without threatening the autonomy or particular profile of the member NGOs.
- 7) The aid allocation formula proposed by Bourguignon and Platteau (2014) is based on an explicit trade-off between needs and governance considerations, as does the formula used by the EU when allocating its aid money between the eligible countries. There are three important differences between the former and the latter, however. First, while the EU formula is computed in a rather ‘ad hoc’ manner, the Bourguignon/Platteau formula is rationally derived from an explicit optimization exercise. This exercise involves an objective function that embeds the needs/governance trade-off confronted by the donor. Second, while the Bourguignon/Platteau formula allows for zero allocation to countries that are too badly governed and not too poor, the formula actually used by the EU does not permit such extreme decisions. This is because political considerations intervene. Third, the mechanism underlying the Bourguignon/Platteau formula allows the donor to affect

the quality of governance in the recipient countries, with the result that poor countries that are initially badly governed can become eligible for aid. This approach nevertheless complicates the choice of appropriate governance indicators to the extent that governance is no more a given but is endogenous to the donor's own efforts.

---

**SUB-TASK 4.3.1 – IfW**

**AN EMPIRICAL ACCOUNT OF THE STRATEGIES OF NEW DONORS**

---

## **1. Introduction**

The increasing importance of donor countries operating outside of the OECD’s Development Assistance Committee (DAC) challenges the existing international aid architecture. These donors may be unwilling to adhere to the rules and procedures of the DAC framework, but may rather follow their own strategies. In particular, non-DAC donors are suspected to provide aid unconditionally without caring about recipients’ governance. Naím (2007), for example, calls China a “rogue” donor only pursuing its economic and political self-interest. China is also the main driving force behind the recently founded BRICS bank<sup>1</sup>, which many see as a potential counterweight to established Western-dominated institutions such as the IMF and the World Bank.

Against this background, our research addresses the following questions: Is the allocation of aid from non-DAC donors significantly different from that of DAC donors? And how do non-DAC donors differ from each other in their aid allocation decisions? While plenty of systematic evidence on aid allocation exists for the group of DAC donors, evidence is scarce for donors outside of the DAC. Taken together, the few previous studies suggest that the aid allocation by “new” and “old” donors appears to be more similar than one might suspect (Dreher et al. 2013). We shed new light on the issue by making use of more recent and comprehensive aid data for non-DAC donors. In doing so, we focus on the three most active donors among the BRICS, namely Brazil, China, and India.

## **2. Data and Methodology**

---

<sup>1</sup> BRICS is an acronym that stands for the five emerging economies **B**razil, **R**ussia, **I**ndia, **C**hina and **S**outh Africa.

Project-level data provided by the AidData initiative (see Tierney et al., 2011) is used to analyze the aid allocation decisions of the three emerging countries. The current version of the database includes 1,008 projects of Brazil's technical development cooperation between 2007 and 2010 and 368 projects of India's development cooperation between 2008 and 2010. Project-level data of China's development cooperation has been collected for Africa based on media reports and other information. The resulting dataset comprises 1,272 projects classified as ODA-like between 2000 and 2012 (Strange et al. 2013).

To determine the aid allocation decision of Brazil, China, and India, a multivariate regression framework is applied. The aid share allocated by these donors to a specific recipient over the period under consideration is used as the dependent variable. We do not exploit the time series dimension of the dependent variable because aid commitments of the three donors exhibit strong volatility from year to year, which cannot be explained by variations in the explanatory variables that are included in the regression. The choice of independent variables follows common practice of the aid allocation literature. Accordingly, they are grouped into three standard categories: recipient needs (poverty; prevalence of disasters), recipient merit (good governance), and donors' commercial (exports; access to resources) and political self-interests. Estimations are performed using the Poisson Pseudo Maximum Likelihood (PPML) approach. This estimator outperforms other estimators such as Tobit and OLS in the presence of heteroscedasticity and many zero observations, which both typically characterize aid data (Santos Silva and Tenreyro 2006).

### 3. Results

A descriptive analysis of the data shows that China spent a large part of its aid budget on economic infrastructure, which is in line with the announced focus of the new BRICS bank. To a lesser extent, this also applies to India, but the projects it supports are mainly related to hydropower in its own region and cross-border connections with a direct benefit for India. A very different pattern emerges for Brazil: It directed only 5 percent its foreign aid to infrastructural projects but 70 percent to projects related to social infrastructure between 2007

and 2010, rendering its sectoral structure of foreign aid more similar to Scandinavia or the United Kingdom than to fellow BRICS.

The econometric analysis reveals for all three countries that political interests play a role in aid allocation decisions. India and Brazil channel a large share of their foreign aid to regional partners, which is in accordance with their claim of being regional leaders. To some extent, they also reach beyond their neighborhood. India seeks for international alliances by putting a focus on less populated countries, while Brazil fosters cooperation with other former Portuguese colonies where it has a comparative advantage through common historical ties and missing language barriers. China isolates Taiwan-recognizing countries by completely excluding them from its development cooperation but gives foreign aid to nearly all Taiwan-rejecting developing or emerging countries. Its broad coverage of recipient countries reflects its ambition to be a global power.

China's foreign aid programs are to a considerable extent driven by access to resources. Between 2000 and 2006 China gave significantly more foreign aid to oil rich countries such as Nigeria and Angola. Between 2006 and 2012, other natural resources than oil became increasingly important as determinants of China's development cooperation in Africa. For Brazil's and India's aid allocation we find no systematic evidence that more foreign aid is channelled to oil and resource rich countries. India however supported large hydropower projects in neighboring countries, and the support was often linked to India receiving future surplus power. Export promotion determines the aid allocation of all three donors, and especially India's.

While political and economic considerations play a significant role, it is unjustified to reduce the BRICS' development cooperation to self-interests. For all countries there is some evidence that they account for recipient need by giving more foreign aid to poorer countries. India and Brazil also give significantly more foreign aid to countries in emergency situations. In contrast to the widely held belief that the emerging donors undermine DAC efforts to reward good governance<sup>2</sup>, our findings suggest that all three donors do not indiscriminately

---

<sup>2</sup> It has to be noted that the efforts of the DAC donors themselves to take governance in recipient countries into account when giving aid is mixed.

support autocratic or otherwise badly governed countries. If anything, the regression results indicate a preference for recipient countries with less corruption, and for democracies in the case of Brazil and India.

All in all, and very similar to what has previously been found for various DAC donors, our empirical analysis suggests that the three BRICS exhibit a mix of selfish and altruistic motives when giving foreign aid.

#### **4. Policy Implications**

Adding new actors to an already fairly complex governance structure with diverging preferences of individual donors will of course further challenge the international aid architecture. Our findings suggest however that the strategies of the three major BRICS donors are not exclusively focused on pursuing economic and political interests. Hence, additional efforts by DAC donors to bring non-DAC donors such as China closer to the mainstream institutional framework - e.g. the DAC itself or the regular high-level meetings of the donor community – in order to agree on joint (minimum) standards in development cooperation may well pay off.

According to our analysis, fears that the non-DAC donors, and the BRICS in particular, are about to establish a rival aid architecture with the BRICS bank as a potential nucleus may be overblown because of these donors' diverse strategies. The announced focus of the BRICS bank on large infrastructural projects, for example, fits quite well with China's foreign aid program today, but is completely at odds with Brazil's. It may well be that the BRICS would be willing to work within the existing multilateral aid system if the international community offered them a fairer representation, e.g. through IMF voting rights that matched their economic potential.

#### **References**

Naím, M. (2007). Rogue Aid. *Foreign Policy* 159 (March/April): 95-96.

Santos Silva, J., and S. Tenreyro (2006). The Log of Gravity. *The Review of Economics and Statistics* 88(4): 641-658.

Strange, A. et al. (2013). China's Development Finance to Africa: A Media-Based Approach to Data Collection. *Center for Global Development - Working Paper* 323.

Tierney, M. J. et al. (2011). More Dollars than Sense: Refining Our Knowledge of Development Finance Using AidData. *World Development* 39(11): 1891-1906.

### **Project-related papers**

Dreher, A., A. Fuchs, and P. Nunnenkamp (2013). New Donors. *International Interactions* 39(3): 402-415.

Semrau, F.O., and R. Thiele (2015). BRICS development cooperation: Why Brazil, China and India give foreign aid and to whom. Unpublished manuscript.

---

#### SUB-TASK 4.3.2 – UNamur

### A THEORETICAL ANALYSIS FOCUSED ON THE ROLE OF NGOS IN AID PROGRAMMES

---

#### 1. SOME STYLISED FACTS ABOUT NGO'S SECTOR: FOUNDATIONS FOR THEORETICAL DEVELOPMENT

The sub-task 4.3.2 intends to analyse the role of NGOs in aid programmes from a pure theoretical perspective. The scientific paper “Development NGOs: Basic Facts” (Aldashev et al., 2014) highlights and discusses a set of nine stylised facts that provide fundamental features of the NGO sector. They concern the size of the development NGO sector and its evolution, the funding of NGOs, the allocation of NGO aid and projects across beneficiary countries, the relationship of NGOs with beneficiaries, and the phenomenon of globalization of development NGOs

**Fact 1.** From the 1950s, there has been a large increase in the size of the development NGO sector, both in terms of the number of organizations and their total revenues. This pattern is driven by increases in the flow of both public and private funds. The visibility and media presence of NGOs has also increased considerably.

**Fact 2.** NGOs increasingly compete for funding; the effect of competition on efficiency and labor composition of NGOs is ambiguous. Most funds are collected by relatively few NGOs. NGOs also compete with for-profit enterprises and specialize/differentiate from them.

**Fact 3.** In certain contexts, NGOs' own funds increasingly dominate public contributions, while in others contexts the opposite is true. Both crowding-in and crowding-out of private donations by public funds is present; however, in the case of Northern development NGOs, most evidence supports the former.

**Fact 4.** NGO aid complements rather than substitutes public aid (with some exceptions). Overall, there are little systematic differences between drivers of NGO aid and

drivers of public channels of aid, but some differences exist when one looks at specific sources of NGO funding.

**Fact 5.** NGOs cluster: both across and within beneficiary countries, NGOs follow other NGOs.

**Fact 6.** The evidence of the impact on beneficiaries is mixed, both on outcomes and targeting. NGOs (Northern and Southern) do not seem to target the poorest communities better than other aid channels.

**Fact 7.** The dependence on donors' funds of both international and local NGOs has several undesirable consequences. The supply-side bias emerges. Accountability is upward, as donors have the power to shape NGO incentives. NGOs face the need to produce visible and measurable outputs, reflecting the "bureaucratization" of the relationship between Northern and Southern NGOs.

**Fact 8.** The relationship between donors and beneficiaries is marked by information asymmetries and requires intermediation. Local intermediaries play a key role in managing these asymmetries. This creates room for rent seeking.

**Fact 9.** NGOs are increasingly internationalized, often assuming a structure similar to multinationals and exploiting brand names, in particular for fundraising purposes.

While interesting per se, these empirical facts allow the development of appropriate theoretical frameworks for modelling the NGO's sector properly. First of all, given the large number of NGOs that compete with each other in multiple dimensions, any plausible model of the NGO sector should go beyond a single-organization analysis and should endogenize the sector market structure. Secondly, the financing structure of NGOs implies a key disconnection between those who pay for the services provided by an NGO and those who benefit from them; thus, a good model should include the intermediation role of the NGOs and cannot avoid addressing the problem of agency (i.e. informational asymmetries between donors and NGOs). This also implies that such models should take into account the strategic interaction between NGOs and donors, in particular, the incentives that NGOs face to get financed which might divert them from their core activities. Finally, theoretical analyses of

the functioning of the sector should provide answers to normative questions, such as welfare trade-offs arising from delegating implementation of development projects to NGOs.

In addition to providing foundations for theoretical development, the facts highlighted in this paper are raising promising research questions on the economics of development NGOs, both from theoretical and empirical perspectives. In terms of policy implications, the conception of an appropriate measure of NGOs performance is discussed. When current measures based solely on inputs (ie. how much money is spent on a given project) appear unsatisfactory, the authors suggest to focus more on measuring output properly through the use of both quantitative and qualitative indicators.

As the data sources and content on the topic were very limited, the set of facts is not exhaustive and some interesting dimensions (ie. the labour composition of the sector) are still missing from the global picture of the NGO's sector presented in this paper.

#### **Related publications or working papers:**

- **Aldashev, G., and C. Nevarra, “Development NGOs: Basic Facts”, CRED Working Paper 1409, 2014**

**Abstract** - This paper systematizes the results of the empirical literature on development non-governmental organizations (NGOs), drawing both from quantitative and qualitative analyses, and constructs a set of basic facts about these organizations. These basic facts concern the size of the development NGO sector and its evolution, the funding of NGOs, the allocation of NGO aid and projects across beneficiary countries, the relationship of NGOs with beneficiaries, and the phenomenon of globalization of development NGOs.

## **2. NGO'S ALLOCATION OF FUNDS: SERVICE PROVISION VS ADVOCACY**

The global agenda for improving foreign aid effectiveness and the increasing role of NGOs in development assistance raise the issue of coordination among organizations

evolving in a fractioned sector. From a theoretical perspective, the paper “Advocacy NGOs” (Morales-Belpaire and Serfilippi, 2015) highlights a counter-intuitive and striking result about coordination of NGO’s advocacy activities. It appears that full-coordination is undesirable in some contexts as it would reduce service provision and hurt beneficiaries. To get a correct grasp of this result, it is necessary to get an overview of the model setting and all the underlying mechanisms.

The theoretical setting corresponds to the case in which NGOs deliver foreign aid in weakly institutionalized countries. It considers funds as given and focuses only on the allocation of funds between two types of activities: poverty alleviating services and advocacy for the rights of the poor. In a context where aid resources may be embezzled by corrupt authorities, advocacy can encourage the local population to demand more transparency from the local authorities with the expected result of reducing embezzlement. The advocacy efforts, however, come at the expense of reduced efforts at directly tackling poverty. In other terms, a trade-off exists between service provision and advocacy. More advocacy would entail improved governance and higher aid effectiveness but also less direct service provision. At the same time, advocacy is subject to under-provision because of its public good nature. Each NGO is expected to reduce its own effort in advocacy as it benefits from the effort in advocacy made by the other NGOs. NGOs can remedy these problems of free-riding by coordinating their actions. However, this coordination threatens the rents of the local authorities and officials will respond to coordination attempts by cracking down on the operations of NGOs. Full coordination is therefore undesirable: crackdown on NGOs will be too strong, which reduces service provision and hurts beneficiaries.

In order to focus on the NGO sector, the behaviour of the government and the local population has been strongly stylized. The assumption that all government officials are pure rent-seekers, or that the local population is a monolithic decision-taking unit are certainly unrealistic. However, by presenting a reduced-form optimization program for the local population and for the government, this model of the political economy of NGOs allows to elaborate on the constraints and strategies adopted by NGOs while maintaining analytical tractability. The results suggest that proponents of a bottom-up approach to development should not go too far in dismissing the role of multilateral and bilateral donors. While merits

of NGOs in the field can be plentiful, they require an enabling environment that allows their initiatives to thrive, while their actions are democratically monitored. Bilateral and multilateral donors have the diplomatic and economic power susceptible of contributing to the establishment of such an enabling environment. This is precisely where the recent work of Bourguignon and Platteau (see below) assumes its importance. They indeed consider the problem of inter-country aid allocation when the donor has the ability to improve governance of the recipient countries.

#### **Related publications or working papers:**

- **Morales-Belpaire, J., and E. Serfilippi, “NGOs under Autocracy”, CRED Working Paper 1413, 2014**

**Abstract** - We develop a theoretical model in which NGOs financed by foreign donors engage in two types of activities in a developing country: service provision and advocacy. In the model, service provision relieves poverty, but these aid resources risk embezzlement by corrupt authorities. Advocacy can encourage the local population to demand more transparency to the authorities, reducing embezzlement at the cost of investing fewer efforts in direct poverty alleviation. We find that in general advocacy will be under-provided because its benefit, improved governance, has the characteristics of a public good. NGOs can remedy to this under-provision by coordinating their actions, but because this coordination threatens the rents of the local authorities, officials will respond to coordination attempts by cracking down on NGOs. Full coordination is therefore undesirable: crackdown of NGOs will be too strong, which reduces service provision and hurts beneficiaries.

### **3. A New Approach to the Role of Development Aid for Poverty Reduction : Trading-off Needs against Governance**

#### **The equity problem: aid darlings and aid orphans**

A criticism that is frequently levelled against the current pattern of aid allocation is the coexistence of 'aid darlings' and 'aid orphans' among recipient countries. It subsists in spite of the coming to the fore of a new approach to development cooperation that emphasized policy

dialogue, country ownership and the need to get rid of conditionalities and reform overload or high transaction costs. Heralded by the Paris Declaration (March 2005) and the Accra Agenda for Action (September 2008), this approach also privileged new aid modalities, General Budget Support (GBS) in particular, considered to be especially suitable to meet the above objectives. Yet, results proved rather disappointing and ex post conditionalities were soon re-introduced, leading to suspension or disruption of GBS in countries such as Nicaragua and Honduras. Donor agencies that are well-known for their rigour, such as SIDA (Sweden) and DFID (United Kingdom), have even decided to give up budget support and return to aid modalities -programmes and projects- that better lend themselves to monitoring and sanction in the event of non-compliance with set conditions.

Because conditionalities associated with GBS are more politically sensitive, arguable and hard to enforce than those associated with project and programme aid (although, as a matter of principle, they should be determined by the recipients' own development priorities), they also tend to cause more frustration among donor agencies with the attendant risk of eventually dropping out the failing countries (Dijkstra, 2013). Not only does such a situation give rise to the aforementioned phenomenon of 'aid darlings' and 'aid orphans', but also, to the extent that the worse-governed countries are generally poorer, it creates a serious equity problem. This is particularly evident in the case of the “zero tolerance for corruption” approach advocated by some in reaction to the uncovering of massive frauds in using aid money in some countries. The fact of the matter is that the number of poor in fragile states where governance problems are the most serious has stayed flat at about 500 million since 1990, and is likely to remain so until 2025 according to a recent study (Sunner, 2012). Since the number of poor in 'non-fragile' states falls quickly –from almost 2 billion people in 1990 to around 500 million now–, countries with weak states will weigh more and more in donors' aid allocation decisions (Kharas and Rogerson, 2012).

### **A new approach integrating needs and governance considerations**

Together with François Bourguignon, previously vice-president of the World Bank, I propose an alternative approach that departs from the above setup. By advocating the need for external discipline imposed by donors in addition to internal discipline inside the recipient

country, this new approach aims at increasing the possibility of rescuing of poor but badly governed countries from neglect. Its advantage lies in the fact that the rescue is effected without going as far as the need-based approach defended by Thirlwall (2011), for example. According to him, indeed, aid assistance should be distributed on a per capita basis according to some target level of per capita income (a principle “which would operate rather like an international negative income tax” (p. 476)). By definition, therefore, the need-based approach does not lend any attention to governance aspects.

We advocate an intermediate approach, labeled “the need-adjusted aid effectiveness” approach. The idea is that the donor’s objective embodies a trade-off between needs and governance considerations: acting as a coordinated body (think of the whole community of donors acting through the UN to meet the MDGs), the donors are concerned not with the amount of aid given to this or that country according to assessment of their needs, but with the amount of aid that actually reaches the poor, which depends on the quality of their domestic or internal governance. This is a satisfactory approach because needs and governance jointly determine which share of the available aid fund should accrue to each potential recipient country.

The donor agency thus faces a choice problem: it must allocate a given amount of aid money between countries heterogeneous in terms of needs and governance. In a two-country setup, this means that one country is relatively poorer and worse-governed than the other. It is because it is sensitive to the share of aid that effectively reaches the target group (the poor) that the donor agency is unavoidably confronted with the aforementioned trade-off between governance and needs when it makes its inter-country allocation decision. The decision criterion that we use is based on the concept of “need-adjusted aid effectiveness”, which precisely reflects such a trade-off. A second essential feature of the new approach is that, when deciding how to allocate aid, the donor allows for the possibility of improving governance in recipient countries, at least with respect to the projects it helps to finance, particularly in the poorer and worse-governed one. Opening up such a possibility through the use of appropriate disciplining instruments –monitoring and punishment– is expected to increase the likelihood that the poorer country will be included in the aid programme.

This expectation is confirmed by our theoretical analysis yet with an important caveat: the disparity in initial governance levels ought not to be too large. In other words, if the quality of governance in the poorer country is too bad relative to that prevailing in the richer country before the donor agency applies its disciplining strategy, then our optimal allocation formula suggests that the poorer country should be denied development aid. If that unfavourable condition is not satisfied, the donor agency distributes a positive amount of aid to both (types of) countries, and the bad governance of the poorer country will be somewhat mitigated by the donor's efforts. On the other hand, if the richer country is too rich compared to the poorer one (the extent of its needs is too small in relative terms), and provided that the quality of governance in the poorer country is not comparatively too bad before the donor agency applies its disciplining strategy, the optimal aid allocation policy requires that only the poorer country receives aid.

Another result that is rather unexpected and again attests to the key role of the initial disparity between the countries' governance levels is the following: the aid share of the poorer and worse-governed country does not necessarily fall when the cost of external discipline increases. Whether it does so or not hinges upon the gap between the countries' initial governance levels. And it is only when such disparity is not too large that allowing the donor's discipline to bear upon inter-country aid allocation has the effect of raising the share of the poorer and worse-governed country.

Inter-country difference in initial governance levels is not the only pivotal variable influencing optimal aid allocation. The behaviour of the costs of external disciplining is equally important. It is thus found that, all other things being equal (including the characteristics of the other recipient country), an improvement in the governance of one country does not necessarily induce the donor to raise its relative share of aid accruing to that country. A key role is actually played by the intensity of the donor's response in terms of external discipline, more precisely by how intensively the donor substitutes better internal governance by less external discipline, possibly over-compensating the gain in internal discipline. The characteristics of the disciplining technology, in particular the monitoring technology available to the donor, matter a lot here: the less sensitive is the cost of that technology to increases in external disciplining the more likely that the intuitive outcome will

prevail: a poorer and worse-governed country is rewarded by a larger share of aid when it has improved its internal governance (irrespective of the donor's efforts toward that end). The intuition is straightforward: if costs are too sensitive, it becomes excessively costly for the donor to improve the governance of the poorer country and to make it a worthwhile recipient of development aid. The policy implication of this result is extremely important: if the technology of monitoring of aid uses by recipient countries is rather ineffective or costly, efforts of the donor community should be directed to innovating this technology in such a way as to make it cheaper and less sensitive to the degree of external discipline desired.

### **The hard challenge of making the aid allocation formula operational**

In the new approach to the role of development aid for poverty reduction, the donor agency has an objective that is defined not only in terms of the intrinsic importance it attaches to the money that effectively reaches the poor but also in terms of the cost of external disciplining. The formula of optimal aid allocation is rather easy to implement as far as the first component of the donor's objective is concerned. Indeed, we only need to collect proper measures of the extent of poverty and quality of governance in potential beneficiary countries. These measures are typically available from international datasets. This is true even for indicators of governance quality. For example, one can use the so-called CPIA indicator which is a Country Policy and Institutional Assessment index that accounts for various aspects of policies and institutions: quality of macro-economic management and policies for social inclusion, quality of institutions and public sector management, and performances of the portfolio of aid projects managed by the World Bank.

The real problem is cost measurement. As a matter of fact, there are no systematic data on the behaviour of the cost of monitoring aid uses and sanctioning bad aid recipients. Till such data become available, we are compelled to simulate different scenarios on the basis of varying assumptions regarding such costs.

Finally, the need-adjusted aid effectiveness approach has important implications with regard to the Performance-Based Allocation (PBA) formula actually used by some multilateral donors to allocate aid. This formula appears to be in agreement with theory in the

sense that the allocation depends positively on needs and governance, although the latter seems to be excessively dominant. However, when governance is allowed to be influenced by the donors through conditionality and disciplining, the ‘need’ component of the formula is called to play a more prominent role. This is precisely the aim of the new approach proposed in this policy brief.

### References:

Dijkstra, G. 2013, “Governance or Poverty Reduction? Assessing Budget Support in Nicaragua”, *Journal of Development Studies*, Vol. 49, Nr.1, pp. 110-124.

Kharas, H. and A. Rogerson, 2012. *Horizon 2025. Creative Destruction in the Aid Industry*. Overseas Development Institute, London.

Thirlwall, A.P., 2011. *Economics of Development -Theory and Evidence*, New York: Palgrave Macmillan (Ninth Edition).

### Related publications or working papers:

- **Bourguignon, F., and J.P. Platteau, “Optimal Discipline in Donor-Recipient Relationships – Reframing the Aid Effectiveness Debate”, CRED and PSE, 2014.**

**Abstract** - Increased attention to the issue of aid effectiveness has sparked a flurry of empirical studies attempting to measure the macro-level impact of aid flows on the performances of developing countries. These studies yield ambiguous and even contradictory results and one possible source of confusion is the fact that they are not grounded in solid theorizing. This paper tries to remedy this lacuna by proposing a principal-agent model in which the donor monitors the use of aid and metes out sanctions in the event of fraud detection. Its most original feature lies in the assumed comparability between internal (domestic) and external (donor-imposed) disciplines and the resulting possibility of studying the behaviour of aggregate discipline. We show that, contrary to intuition, an (exogenous) improvement of domestic discipline may be over-compensated by the donor so that total discipline actually decreases and elite capture paradoxically increases. This implies that the relationship between domestic and total disciplines may be non-monotonous. We highlight the crucial role of the shape of the cost functions to obtain not only the above paradox but also corner solutions in which the donor optimally chooses to refrain from imposing any external discipline. The central lesson to draw from the whole exercise is therefore that no simple general testable prediction can be inferred from economic theory regarding the impact of aid on the donors' objective even when the quality of domestic governance or the policy environment is considered.

- **Bourguignon, F., and J.P. Platteau, “Aid Effectiveness Revisited: The Trade-Off Between Needs and Governance”, CRED and PSE, 2014.**

**Abstract** - The paper proposes an approach centered on the concept of need-adjusted aid effectiveness. This means that the donor's objective function explicitly takes into account the trade-off between considerations of needs and considerations of governance. Moreover, the donor is willing to exert external discipline on the recipient countries. To the extent there is a negative correlation between the extent of needs and the quality of governance, we expect that the donor would bring more discipline to bear upon the poorer countries with the consequence that they would not be excluded from aid programmes. Working within a one-donor-two-recipient framework, in which one recipient country is relatively poorer and worse-governed than the other, we are able to show that many intuitions regarding effects of parametric changes are too simple. In particular, the improvement in the governance of the poorer country does not necessarily induce the donor to raise its aid share.

#### **4. Theoretical investigation of the impact of internationalized competition in fundraising on the NGO sector**

Starting from the stylized facts described above - namely Fact 1 (increasing size of the NGO sector), Fact 2 (intensified competition for funding for NGOs), Fact 5 (NGOs cluster), Fact 9 (internationalization of NGOs), it appears crucial to get a better understanding of the drivers and the consequences of the internationalization process of the NGOs sector on the NGOs' capacity to raise fund and on the effectiveness of their development activities. Several theoretical papers developed notably by G. Aldashev (CRED, UNamur) and co-authors specifically focus on this question and provide rich answers.

##### **When NGOs go global**

A first question that arises is why the NGO sector is more and more concentrated into large multinational entities and subsequently what it implies in terms of social welfare. Aldashev and Verdier (2009) address this question by using an international trade model of two countries with horizontally differentiated NGOs competing in fundraising. They find that large economies of scale in the fundraising activities can explain the formation of large

multinational NGOs and the disappearance of smaller NGOs. The shift towards a more internationalized and concentrated sector was observed between 1970 and 1990. The authors discuss this shift in the light of the emergence in the 70s of humanitarian aid agencies: large humanitarian crises, together with the massive use of large scale media technologies for fundraising have dramatically increased the returns to scale in fundraising. Finally, the authors show that this move from a world of small local NGOs to a world of internationally concentrated NGOs is welfare improving, meaning that it allows to raise more funds and thus to care for more beneficiaries.

### **Related publications or working papers:**

- **Aldashev, G. and T. Verdier, “When NGOs Go Global: Competition on International Markets for Development Donations”, *Journal of International Economics*, 2009, vol. 79(2): 198-210**

**Abstract** - Why are many large non-governmental organizations (NGOs) becoming multinational entities? What are the welfare implications of this integration of markets for development donations? To answer these questions, we build a simple two-country model with horizontally differentiated NGOs competing in fundraising. We find that NGOs become multinational if the economies of scale in fundraising are sufficiently large. In that case, national NGOs in the smaller country disappear, while some national NGOs remain in the larger country only if country sizes are sufficiently different. Social welfare is higher in the regime with multinationals than under autarky.

### **NGO competition and coordination in fundraising**

As already stressed in the stylized Fact 2, NGOs are increasingly competing for fundraising. This has consequences for the sector structure, size and on the efficiency of their core activity: development projects.

The time spent by a NGO on fundraising activities is taken away from time invested in development projects. Simultaneously, smaller fundraising activities reduce the possibility to finance development projects. There is thus a clear trade-off faced by NGOs. Aldashev and Verdier (2010) analyze how the competition for funds between NGOs affect their behavior and the market structure, based on a model of competition among horizontally-differentiated NGOs. They find that when the number of private donors is fixed (fixed market size), a more intense competition between NGOs increases the levels of fundraising, which, in turn,

increases the welfare of donors. For beneficiaries, more NGOs on the markets can have two effects on their welfare: 1/ positive through a greater variety of development projects, 2/ negative because an additional NGO has a negative effect on the impact of the previously existing NGOs. The latter effect is driven by the fact that in a fixed size market, the fundraising activity of one NGO can decrease the donations received by another NGO (negative externalities). Hence competition in donations – when the aggregate amount of donations is relatively inelastic to fundraising – can be socially wasteful. However, these welfare implications change when the size of the donations market is not fixed but is determined by the fundraising intensity (endogenous): a more intense competition for donations leads to lower levels of fundraising. Understanding how effective efforts are in attracting new donors is therefore crucial to know whether the market size is fixed or not.

Increased competition on the donation market can be socially undesirable. Therefore, Aldashev *et al.* (2014) analyze under which conditions cooperation between NGOs can be sustained and desirable. The authors rely on a model of endogenous nonprofit alliance formation. Since the fundraising activity of one NGO can affect the donations received by another NGO, NGOs are imposing negative externalities on each other's output. Under what conditions can NGOs form a coalition in which they commit to levels of fundraising that internalize these externalities? The stability of such coordination is determined by three key characteristics: 1/ the alliance formation rule, 2/ whether the deviation from a given agreement can be done by a single NGO only or by a group of NGOs within the coalition, and 3/ the extent to which fundraising efforts of a given NGO are positively or negatively affected by the efforts of others NGOs. Sustainability is weakened when projects proposed by NGOs are quite differentiated, e.g. donors have poor information about a new cause espoused by a NGO which is therefore in doubt about the donors potentially interested. However, when donors are familiar with the projects of NGOs and consider the various NGO as forming a similar group (e.g. in the case of a large humanitarian emergency), cooperation can be sustained.

#### **Related publications or working papers:**

- Aldashev, G. and T. Verdier, “Goodwill Bazaar: NGO Competition and Giving to Development”, *Journal of Development Economics*, 2010, vol. 91(1): 48-63

**Abstract** - This paper builds a model of competition through fundraising between horizontally differentiated NGOs. NGOs allocate their time resource between working on the project and fundraising, which attracts private donations. If the market size is fixed, the fundraising levels increase with the number of NGOs and the free-entry equilibrium number of NGOs can be larger or smaller than the socially optimal number, depending on the efficiency of the fundraising technology. If the market size is endogenous and NGOs cooperate in attracting new donors, fundraising levels decrease with the number of NGOs and the free-entry equilibrium number of NGOs is smaller than the one that maximizes the welfare of donors and beneficiaries. If NGOs can divert funds for private use, multiple equilibria (with high diversion and no diversion of funds) appear.

- **Aldashev G., M. Marini and T. Verdier, “Brothers in Alms? Coordination between Nonprofits on Markets for Donations”, *Journal of Public Economics*, 2014, vol. 117(1): 182-200**

**Abstract** - Mission-driven nonprofit organizations compete for donations through fundraising activities. Such competition can lead to inefficient outcomes, if nonprofits impose externalities on each others' output. This paper studies the sustainability of fundraising coordination agreements, using a game-theoretic model of coalition formation. We show that three key characteristics determine the stability of cooperation between nonprofits: (i) the alliance formation rule, (ii) the extent to which fundraising efforts are strategic complements/substitutes, and (iii) whether deviation from the agreements is by an individual or by a group of nonprofits. We analyze how the interaction of these three features induces (or not) the stability of Pareto-optimal full coordination in fundraising.

### **When NGOs are (not) monitored and when NGOs monitor**

The economic globalization is affecting multiple dimensions of NGOs: not only the structure of the market and the size of the NGOs as described above, but also their targeted development activity and the type of workers they are attracting, for instance.

Globalization does not only affect NGOs through the increased competition for funding but it also pushes NGOs to invest more in activism aimed at monitoring social-responsible actions of large multinational firms. Aldashev, Limardi and Verdier (2015) investigate how NGOs' activism interacts with the industry structure. They build a game-theoretic model of interaction between a NGO and a firm, in which the NGO monitors the adoption by firms of socially responsible actions. The model brings some light on the key empirical patterns observed in industries under activist pressure in developing countries: 1/ the exit from the industry under scrutiny increases as activists pressure grows, 2/ the response

of industries to NGOs' activism is heterogeneous, depending on their genuine commitment to special objectives, 3/ NGOs' activism increases following globalization.

Another interesting question is how a lack of monitoring of the use of funds, i.e. when donors do not control how funds are used, can affect who is willing to work in the non-profit sector and ultimately how well the sector is performing. Aldashev, Jaimovich and Verdier (2015) investigate this question based on a general-equilibrium framework of occupational choice with for-profit and non-profit sectors and endogenous private donations.

They show that when the use of funds is not totally monitored, an increase in the funds of the non-profit sector can impede the capacity of the NGOs to attract motivated workers and subsequently, worsens the performance of the non-profit sector. Foreign aid intermediation through the non-profit sector in a developing country can therefore entail perverse effects. For instance, a large injection of foreign aid can attract self-interested agents into the non-profit sector which, as a result, suffers from a lower average motivation among its workers. Lastly, they show that a properly designed public financing policy of the non-profit sector can improve the motivational composition of the non-profit sector. Taxation alters the occupational choices via two channels: it reduces the returns in the private sector and it increases the aggregate transfers to the non-profit sector. If public financing is able to raise the aggregate funding of the non-profit sector, while at the same time sufficiently increasing the number of non-profit managers (so that the funding that each non-profit firm obtains is actually lower), this policy will lead to the entry of motivated agents and the exit of unmotivated ones from the non-profit sector.

#### **Related publications or working papers:**

- **Aldashev G., M. Limardi and T. Verdier, "Watchdogs of the Invisible Hands: NGO Monitoring and Industry Equilibrium", *Journal of Development Economics*, 2015, 116(1): 28–42**

**Abstract** - Globalization has been accompanied by rising pressure from advocacy non-governmental organizations (NGOs) on multinational firms to act in socially-responsible manner. We analyze how NGO pressure interacts with industry structure, using a simple model of NGO-firm interaction embedded in an industry environment with endogenous markups and entry. We explain three key empirical patterns in developing-country industries under activist pressure: the degree of exit

under more intense activist pressure, the differential response of industries to NGO activism, and the general rise of NGO activism following globalization.

- **Aldashev G., E.Jaimovich and T. Verdier “When Warm Glow Burns: Motivation (Mis-)Allocation in the Nonprofit Sector”, working paper version: Feb. 2015**

**Abstract** - We build a general-equilibrium model of an economy with the non-profit sector through private warm-glow donations. Lack of monitoring on the use of funds implies that an increase of funds of the non-profit sector (because of a higher income in the for-profit sector, a stronger preference for giving, or an inflow of foreign aid) worsens the motivational composition and performance of the non-profit sector. If motivated donors give more than unmotivated ones, there exist two stable (motivational) equilibria. Linking donations to the motivational composition of the non-profit sector or a tax-financed public funding of non-profits can eliminate the bad equilibrium.

---

### SUB-TASK 4.3.3 – EGAP

#### A COMPARATIVE CASE STUDY TO ASSESS THE PERFORMANCE OF NGO

---

**Objective:** Assessment of the performance of CSO's, in particular the impact of funding rules on Civil Society Organization's empowerment, and their ability to achieve sustainable impact.

**Researcher/partner:** Marta Ochman, Escuela de Gobierno, Tecnológico de Monterrey, Mexico

**Contributors:** Ingrid Sada, Tecnológico de Monterrey; Ana Villafuerte

**Context, rationale and interest of research:** The objective of the investigation is to analyze the impact of funding rules on the capacity of Civil Society Organizations (CSO) to achieve long-term objectives (development, empowerment of communities). The initial hypothesis was that, there is a contradiction between the requirements and rules of the donors, and the capacity of CSOs to achieve an impact on development, because of the following reasons:

1. The CSOs must adjust their agendas and methodologies to meet donors' preferences, donors who frequently follow trending ideologies and prefer so called *tested solutions*. The persistence of marginalization and exclusion, despite the development policies implemented back in the 50s, demonstrates the need of new and innovative strategies. Funding rules make very little room for innovation.
2. Evaluation guidelines established by donors only seek to audit granted resources, and they don't evaluate the long-term impact.
3. The emphasis of donors in the professionalization of organizations entails tension between the technical and managing capabilities of being competitive in calls,

and the abilities to work with communities or grassroots organizations (local knowledge and sensibility to communities' customs).

4. Funding has a short temporal horizon; while development processes are long-range.

Since the study is qualitative, it focuses on Mexico, but we consider that its findings may be applied to middle income countries, for which there is less availability of external resources, hence, the CSOs depend on internal donors, may them be enterprises or governments.

**Methodology:** The study has been developed with a qualitative method. Through a bibliographic review, we identified the analytic category that allows describing the social reality that we seek to observe (capacity of CSOs to promote development). This theoretical construct is *empowerment*, defined as a constant and intentional process that allows people, organizations and communities to gain more control over the issues that affect them, through a major access to resources, acquisition of new abilities and improvement of their status within society. (Perkins and Zimmerman, 1995; Young, 1998). Particularly, we decided to observe the organizational empowerment, for -being an intermediate level-, organizational empowerment mediate between personal and community empowerment (Kroecker, 1995; Rifkin, 2003; Speer and Hughey, 1995; Peterson and Zimmerman, 2004). Also, many authors establish the direct relation between the organizational empowerment and the development approach (Kroecker, 1995; Datta and Kornberg, 2002).

On this theoretical category (organizational empowerment), directly observable indicators were built, which were the basis for the development of scripts for semi-structured interviews. The interviews were conducted between September and December 2014, in nine organizations (13 people) with different profiles, from community organizations, such as *Las Gaviotas* or *Red de Mujeres de Bajío*, to international ones, such as OXFAM or YMCA. A public officer was also interviewed, who is responsible for the articulation of the Government of Guanajuato with the Civil Society Organizations. All interviews were recorded and transcribed for encoding.

## **Main Results:**

1. Among donors dominates the neo-liberal vision of the role of Civil Society Organizations, as more efficient providers of basic services. In addition, both the Governments and enterprises, use funded CSOs for their own political or marketing purposes. On the other hand, CSOs have internalized the “third sector” discourse, i.e. they see themselves as actors that must be autonomous from both the State and the Market. They accept efficiency demands as a condition to access funding, but they defend their right to autonomy.
2. Donors don't understand clearly the concept of development, nor do they distinguish between development strategies and strategies to fight poverty. As a result, during tenders or calls to allocate resources, they talk about development objectives, but technical terms and conditions to access those resources, are befitting to welfare projects. Particularly:
  - a. The overwhelming majority of projects are short-term (between 6 and 8 months), and involve either training or direct delivery of resources. Even in long-term projects, the transition period, in which the organization is removed from the community, but needs to keep monitoring and advisory mechanisms, is not funded.
  - b. The evaluation process doesn't consider impact on development, the main interest to audit the use of granted resources.
  - c. There is a tendency of payment by results; donors do not consider the complexity of the socio-political context, even of insecurity faced by organizations that work in and with the marginalized communities. They see the problem in a linear way: lack of development => applied resources => higher degree of development.
3. The CSOs work in an environment that inhibits innovation:
  - a. Frequently, donors consider CSOs as mere implementers of their preferences and programs, designed without the participation of the CSOs or potentially benefitted communities in the design of strategies.
  - b. Only the implementation of projects is financed. The diagnosis, design and pilot stages must be funded by organizations.

- c. All organizations, even those with a long career and high capacity to compete for resources, live the daily struggle of paying administrative expenses, basic conditions for the survival of the organization.
- d. The dynamics of competition for resources and the processes of design and implementation of projects leave little time for activities that promote innovation, like the processes systematization, exchange of experiences, renegotiation of funding rules. These activities depend on the availability of resources specifically provided for these purposes.
- e. Donors ask for cooperation and networking or alliances among the different organizations, but they see it as a strategy to improve administrative efficiency and achieve a greater quantitative impact, not as a strategy to promote organizational learning and innovation.
- f. Access to external funding is particularly difficult for new or community organizations, this limits the diversity of actors present in the debate and in the practice of development-oriented projects.

Particularly for Mexico, the following negative phenomena have been identified:

1. The recent tax reform in Mexico has had a catastrophic impact on community organizations, and endangers the ability of intermediate organizations to promote local networks of suppliers.
2. Funding from the Mexican Government highly depends on political dynamics, and especially at the local level, it is immersed in corruption networks.
3. Organizations that have experience with international and national donors, consider that procedures required by Mexican donors are heavier and more expensive than those required by international donors (European or American).

The main dynamics that makes a significant contribution to development is the collaboration between more professionalized and consolidated organizations with community based organizations or directly with communities. These intermediate organizations assume characteristics of second-tier foundations, for their ability to capture and channel resources. But unlike second-tier foundations or consulting firms dedicated to capture resources, they have a long tradition of fieldwork, a clearer vision of what community development is, and civil society logic, not market logic. These organizations have a long-term commitment with

communities, hence, they also assume the costs of obtaining a sustainable funding, fulfilling administrative and fiscal requirements established by donors, which are impossible to fulfill by small organizations.

Other strategies implemented by CSOs to maintain their autonomy and to implement projects they consider unprofitable or not so attractive for donors, but important to promote development, are:

1. Reduce the dependence on institutional funding creating a base of individual contributors, who do not label resources, so that they can be used for administrative expenses, design of new projects, pilot projects, etc.
2. Establish trustful relationships with institutional donors through personal contact and involvement in projects and with benefitted communities. This also entails a long-term relationship with the donors (renewed funding).
3. Combine fidelity to program objectives and own projects/strategies, with a discursive adjustment to donors' priorities.
4. Apply Strategies of *creative accounting* to ensure minimal resources of organizational sustainability.
5. Search for collaboration with universities, to share the cost of diagnosis, evaluation and accompaniment; or also as sources of volunteers (social service programs).

**Policy implications:** For policy recommendations, we consider two scenarios.

Scenario 1: The European Union maintains its current policy of removing the funding of direct projects and focus on supporting institutional strengthening programs, within the framework of the intergovernmental policy dialogue. In this case, the recommendations are:

1. In the case of the institutional strengthening program, The EU should:
  - 1.1 Support the revision process of fiscal policy, currently centered on increasing the fiscal capacity and prevent money laundering. Advisory and funding are both needed to make possible a participatory process, that allows to include the concerns and interests of Civil Society Organizations, in particular, to establish conditions that

do not benefit social enterprises over community organizations or over the ones that work on development projects.

1.2 Insist on transparency mechanisms in the allocation of resources to CSOs. It is necessary to work mostly at the local level (municipalities and States), where corruption and political conditioning of resources are deeply rooted.

1.3 Invest in programs to strengthen municipalities on transparency and accountability processes, but also their capacity to work together with local CSOs and communities in development projects.

1.4 Promote and advise a process of administrative simplification for the public tenders through which resources are granted to CSOs.

2. The Laboratory of Social Cohesion European Union – Mexico (LSC) must:

2.1 Promote a debate on the difference between development and welfare projects, as well as the particular conditions required by development projects (multi-year funding, evaluation that considers the complexity of both the social and political context, funding for organizational sustainability). There is also necessary to develop strategy so that this knowledge is well socialized among public administration, and between social actors, including enterprises.

2.2 LSC should not to invest in workshops to strengthen the capacity of CSOs to compete for governmental resources, for this kind of training is widely offered. The workshops should focus on:

a. Designing qualitative indicators of social impact of the projects, as well as strategies to socialize these methodologies among donors.

b. Increasing the capacity of CSOs to increase funding through individual donors, those who allow greater autonomy in decision-making on the resources.

2.3 Support CSOs advocacy to revise legislative framework, such as la Ley de Fomento a las Actividades Realizadas por las Organizaciones de la Sociedad Civil. This strategy must include funding for advocacy networks and grassroots lobbying.

2.4 The hub of scientific and technical cooperation offers an area of opportunity to strengthen cooperation between universities and CSOs. There is a widespread perception that universities can support the design of innovative methodologies for both intervention and evaluation of development projects. It would be positive to

establish financing funds for applied research in joint projects between educational institutions and civil society organizations.

Scenario 2: The European Union revises its international cooperation policy for middle-income countries, and increases the resources for direct funding of CSO's projects.

We consider that it is a desirable scenario that will allow greater impact on social cohesion. Although, it is true that Governments and corporate actors in middle-income countries have sufficient resources to promote development, in the medium term, we can't expect radical changes in the culture of corruption and political use of resources.

Bearing in mind that the cooperation policy is reviewed every 6 years (in the case of Mexico) there are mechanisms to review periodically the progress in terms of institutional strengthening (Scenario 1 recommendations).

To make the direct funding of projects fit the requirement of a strategic approach (major visibility of the impact), it is recommended, above all, to review and systematize the priority regions for social investment. Currently, the European Union investment focuses on Chiapas and on the northern region, like Chihuahua (Ciudad Juárez). Those are targets of incidence that reflect a context from 10-20 years ago. Although they keep on being regions with problems of poverty and inequality, the EU should focus its investment on regions that are not strategic to the United States. The northern region, due to its proximity with the United States, as well as the States that drive out more migrants to the northern neighbor (Guanajuato, Michoacán) have greater ability to raise resources from U.S. based foundations and organizations. There are also regions where there is already a strong presence of Mexican consolidated CSOs. It is important to make a diagnosis that gives visibility to regions that face problems such as poverty and political corruption, like Guerrero, to strengthen the empowerment of communities, including the culture of peace and productive projects.

**This investigation added value:**

1. The investigation has involved intensive fieldwork, which draws real expertise from organizations that deal with the issue of development.

2. Although the research was conducted in Mexico, the recommendations are transferable not only to other middle-income countries, but also to low income countries.